Supreme Court, U.S.
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No. 87-2032

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

THOMAS E. LILLY,

Petitioner,

vs.

EBSCO INDUSTRIES, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

RESPONDENT EBSCO INDUSTRIES, INC.'S BRIEF IN OPPOSITION

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QUESTION PRESENTED FOR REVIEW

Whether a district court, within its discretion, may issue a preliminary injunction restricting the disposition of a defendant's assets where:

1. The unrefuted evidence demonstrates the defendant's embezzlement and breach of fiduciary duties;
2. The defendant stipulates that the plaintiff has a substantial likelihood of success on the merits of all its claims;
3. The plaintiff seeks an accounting from the defendant;
4. The evidence shows the defendant's transfer and dissipation of assets;
5. The defendant invokes his Fifth Amendment privilege upon deposition, and fails to attend the preliminary injunction hearing; and,
6. Available state pre-judgment attachment remedies do not provide plaintiff with an adequate remedy at law.

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Respondent, EBSCO Industries, Inc., respectfully requests that this Court deny the Petition for Writ of Certiorari seeking review of the Order of the United States Court of Appeals for the Sixth Circuit in this case.

STATEMENT OF THE CASE

This is an action for fraud, material breach of representations, breach of contract, negligence, breach of fiduciary duty, and for an accounting by EBSCO Industries, Inc. (EBSCO) against Thomas E. Lilly (Lilly), arising out of the sale of the assets of Four Seasons Garment Corporation (Four Seasons) to EBSCO by Lilly, and out of Lilly's activities as Vice President of EBSCO and General Manager of Four

Seasons following that sale. Evidence presented at the May 22, 1986 hearing on EBSCO's Motion for Preliminary Injunction established the following facts.

Four Seasons was a Mason, Ohio manufacturer/wholesaler of custom sporting and leisure apparel. EBSCO is a diversified Birmingham, Alabama based company with interests in subscription reading services, printing, advertising displays, publishing and various other products and services. On December 6, 1983, EBSCO purchased certain assets and the name of Four Seasons from Lilly and his associates. (R. 44, Ex. 1). At that time, Lilly owned the majority of Four Seasons stock, and was the Chairman of its Board of Directors. Under the agreement, Lilly and his associates were to remain at Four Seasons under consulting agreements, and were to operate the company as a division of EBSCO. The sellers also entered into extensive agreements not to compete with EBSCO. (R. 44, Exs. 2-4).

The acquisition did not include purchase of Four Seasons' accounts receivable. (R. 44, Ex. 1; R. 44 at 32). On the eve of the closing, Lilly approached EBSCO with the proposal that EBSCO lend Four Seasons and Lilly Three Million Dollars to be used to satisfy their obligations to the First National Bank of Boston to which the receivables were pledged. (R. 44 at 33-34). It was represented to EBSCO that the receivables had a value of approximately Five and one half Million Dollars. (R. 44 at 33-34). Based upon this representation and upon a written certification that the accounts receivable were not less than Four Million Nine Hundred Thousand Dollars, EBSCO lent Three Million Dollars to Four Seasons Garment Corporation in return for a promissory note from that corporation, guaranteed by Lilly. (R. 44 at 34; R. 44, Exs. 5, 10-13). Under the agreement, Lilly was to retire the note by monthly installments equal to the payments received upon such accounts receivable in each month. (R. 44 at 37-38).

Unknown to EBSCO, Lilly had knowingly overstated the Four Seasons accounts receivable by approximately Four Million Dollars, by creating fictitious accounts in order to ob-

tain the financing that his loan from EBSCO was to pay off. (R. 44 at 86-89). Since there were not enough actual receivables to retire the note, Lilly contrived a scheme of embezzlement to perpetuate and conceal his original fraud. Under this scheme, he applied Two Million Seven Hundred Thousand Dollars in receipts from accounts generated *after* EBSCO's purchase to retire the Three Million Dollar note; *thus paying EBSCO with its own money*. (R. 44 at 43, 62, 84-86; R. 44 Ex. 28). To do this he submitted monthly reports to EBSCO in which he personally falsified the amount of income alleged to be from the "old" accounts. (R. 44 at 40-41, 89-90; R. 44, Ex. 29).

After all payments on the note were made, Lilly's fraud continued. Since he had used current income to satisfy an antecedent obligation, he had to persist in creating fictitious accounts receivable and inventory to avoid disclosure that the business was losing money, and that the receivables had been misapplied. (R. 44 at 40-41, 89-90; Ex. 29). This was done by Lilly in several ways.

First, by conspiring with an outside computer consultant and others, the company data processing system was manipulated to accept and print a false accounts receivable list. (R. 44 at 42, 91-92). Second, Lilly and others produced bogus invoices and other documents which confirmed the false accounts receivable print-out and misled auditors. (R. 44 at 89-92). Third, Lilly arranged for many of the outside auditors' accounts receivable confirmations to be sent to and returned by persons acting on Lilly's instruction (R. 44 at 42).

Lilly's fraud collapsed in the last few days of March, 1986. Unable to convince one of his involved associates, Richard Egan, to participate any longer, Lilly cleaned out his office and departed on March 31, 1986. Egan then went to EBSCO management and described the wrongdoing in great detail. (R. 44 at 43-44).

EBSCO's efforts to obtain discovery from Lilly were frustrated by his invocation of the Fifth Amendment privilege

against self-incrimination. (R. 22). However, EBSCO was able to determine that Lilly had liquidated his securities holdings and had transferred the proceeds therefrom to a Memphis, Tennessee liquor store owned in part by Lilly, and operated by his brother-in-law, Lewis Harris. From there much of the money was taken out by Mr. Harris. (R. 44, Exs. 30-36).

Testimony of J. Edward Porter indicated that, one week prior to his departure, Lilly stated that he had a "safe place" to transfer funds if found out by EBSCO. That "place" was described as Barbara Harris, Lewis Harris' wife. (R. 44 at 72).

The final items of evidence were records of Society Bank, the admissibility of which was stipulated. Those records disclosed Lilly's unauthorized withdrawal of funds from Midwest Skyline, Inc. and their deposit in Design Masters, another business of Lilly's. These documents were introduced as evidence of Lilly's past dissipation of funds to which he was not entitled and were probative of EBSCO's entitlement to the relief granted by the district court.

Based upon the evidence, the district court issued its Preliminary Injunction (R. 24) and subsequent Findings of Fact and Conclusions of Law (R. 41). The Court of Appeals affirmed.

REASONS FOR DENYING THE WRIT

Petitioner herein essentially adopts and urges the correctness of the dissenting opinion in the Sixth Circuit. The gist of that dissent is that a defendant's pre-judgment disposition of assets may be enjoined *only* if those assets comprise a readily identifiable *res* which is subject to the ultimate relief of a constructive trust. Lacking such a *res*, the dissent reasoned, Respondent has an adequate remedy at law pursuant to Rule 64 of the Federal Rules of Civil Procedure and Ohio Revised Code § 2715.01, *et. seq.*

The flaw in this argument is that it focuses the determination of the adequacy of legal remedy upon the fortuitous existence of an immediately identifiable *res*, rather than upon the various shortcomings of Ohio's pre-judgment attachment statutes under the circumstances of this case. Indeed, had such a *res* been identifiable, Respondent may have been able to obtain it without the need for equitable relief. It does not logically follow, however, that injunctive relief is only available when it is not needed.

As pointed out by the majority below, Ohio's pre-judgment attachment system:

1. Cannot apply to assets outside Ohio;
2. Requires that securities be garnished by the actual levy upon stock certificates; and,
3. Involves unavoidable delays.

Additionally, under the attachment statutes, the party seeking attachment must submit an affidavit setting forth a description of the property, the location of the property, and the use to which it is being put. Ohio Revised Code § 2715.03(E). Obviously, this could not be accomplished here, where the undisputed evidence revealed a pattern of liquidation and transfer of assets out of Ohio.

Despite Petitioner's argument to the contrary, no decision of this Court precludes or counsels against the preliminary in-

junction herein, and no decision of another Circuit has reached a conflicting determination.

Petitioner has cited several Supreme Court and Circuit Court cases in support of its proposition. *DeBeers Consol. Mines* v. *United States*, 325 U.S. 212 (1945), *Phoenix Mutual Life Ins. Co.* v. *Bailey*, 80 U.S. (13 Wall) 616 (1871), *Adler* v. *Fenton*, 65 U.S. 407 (1861), *Martin* v. *James B. Berry Sons Co., Inc.*, 83 F.2d 857 (1st Cir. 1936), *Wahlgren* v. *Bausch & Lomb Optical Co.*, 77 F.2d 121 (7th Cir. 1935), *Friedling* v. *Freedman*, 44 App. D.C. 191 (1915). However, none of these decision deals, as here, with a claim for an accounting; or with actual as opposed to potential, dissipation of assets; or with a stipulated likelihood of success on the merits; or with the demonstrated inadequacy of state attachment proceedings to effect relief.

Moreover, this Court has recognized that under appropriate circumstances, a district court may enjoin a party from the disposition of property under that party's control. *United States* v. *First National City Bank*, 379 U.S. 378 (1965). Respondent submits that the within circumstances clearly meet the test set forth therein.

The decision below raises no important question of federal law or procedure. It is well established that a district court, sitting in Equity, has broad discretion to apply its injunctive powers. It is likewise clear from the facts herein, that the district court properly responded to a peculiar situation not normally found in routine tort or commercial claims. Indeed, it is the very flexibility of Equity which permitted the district court to fashion the remedy of which Petitioner complains. The promulgation of rigid restrictions upon this flexibility is neither warranted on these facts nor desirable in the abstract.

CONCLUSION

For the reasons set forth above, Respondent, EBSCO Industries, Inc., submits that the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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